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ZNR UUUUU ZZH
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FM AMEMBASSY PRETORIA
TO RUEHC/SECSTATE WASHDC 3778
INFO RUCNSAD/SOUTHERN AFRICAN DEVELOPMENT COMMUNITY
RUCPCIM/CIMS NTDB WASHDC
RUCPDC/DEPT OF COMMERCE WASHDC
RUEATRS/DEPT OF TREASURY WASHDC

UNCLAS SECTION 01 OF 03 PRETORIA 002261

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DEPT FOR AF/S/MTABLER-STONE; AF/EPS; EB/IFD/OMA
USDOC FOR 4510/ITA/MAC/AME/OA/DIEMOND
TREASURY FOR OAISA/RALYEA/CUSHMAN
USTR FOR COLEMAN

E.O. 12958: N/A
TAGS: ECON EINV EFIN ETRD BEXP KTDB PGOV SF
SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER JUNE 2 2006
ISSUE

¶1. Summary. Each week, Embassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:

- First Quarter GDP Growth Accelerates;
- April Credit Growth Slows;
- China, SA Conclude Draft Agreement to Restrict Textile Exports;
- SA Trade Deficit Reaches R2.4 Billion;
- Koeberg's Unit 1 Operational;
- Eskom Spending a Brake on Increased SA Growth; and
- Manufacturing Recovers.

End Summary.

First Quarter GDP Growth Accelerates

¶2. Economic growth accelerated to 4.2% in the first quarter 2006, after 3.2% growth during the last quarter 2005, according to Statistics SA. First quarter 2006 growth was the 30th consecutive quarter of economic growth, the longest continuous growth phase in South Africa's history. The highest growing sector was the construction sector, which, although it makes up only 2.8% of total output, grew 13.7%, compared to 12.4% during the fourth quarter 2005. The manufacturing sector showed a sharp improvement, growing by 4.3% compared to 4th quarter 2005 contraction of 0.3%. Other sectors showing substantially higher growth in the first quarter 2006 include the finance and real estate at 8.8% compared to fourth quarter 2005 growth of 3.7%. The finance sector makes up 19.5% of South Africa's economy. However, the primary sectors of the economy, agriculture and mining, contracted. The mining sector, which contributes 6.3% of GDP, declined only 2.9% compared to fourth quarter's decline of 5.4%. Despite the commodities boom, the mining sector is now officially in recession, having contracted for three consecutive quarters, by 3.4% and 5.4% in the last two quarters 2005 and by 2.9% in the first quarter
¶2006. Table 1 shows growth rates in the first quarter 2006 and fourth quarter 2005 for South Africa's major industrial sectors and indicates that the services sector continues to fuel South Africa's GDP growth.

Table 1.

Quarterly Growth,	Fourth Quarter 2005	First Quarter 2006
Primary Sector	-2.7%	-4.1%

Agriculture	3.9%	-6.9%
Mining	-5.4%	-2.9%
Secondary Sector	1.7%	5.5%
Manufacturing	-0.3%	4.3%
Electricity/Water	3.5%	3.6%
Construction	12.4%	13.7%
Services Sector	3.2%	4.2%
Wholesale/Retail Trade	9.0%	5.1%
Transport/Communication	6.5%	4.9%
Finance/Real Estate	3.7%	8.8%
Personal Services	2.9%	3.4%
Government	1.9%	1.2%
GDP	3.2%	4.2%

Source: Investec's GDP Update, May 30; Business Day and Business Report, May 31.

April Credit Growth Slows

¶3. Growth in M3, the broadest measure of money supply, slowed to 23% (y/y) compared to March's growth of 26.8%. Growth in private sector credit extension (PSCE) slowed to 23.2% y/y in April, from 24.3% during March. Installment sales credit increased by R1.7 billion, or 18.4% y/y, and leasing finance rose by R741 million. Mortgage advances were up R11 billion, showing a 30.1% y/y increase. Other loans and advances, mainly corporate overdrafts and credit card debt, slowed to a growth rate of 15.6% (18.8% previously). JPMorgan economist Marisa Fassler expects the South African Reserve Bank (SARB) to increase interest rates by 25 basis points, especially if the SARB's inflation forecasts were revised upwards to reflect a weaker rand and the second quarter inflation expectations came in higher due to higher petrol prices over the past few months. The SARB's Monetary Policy Committee meets on

June 7 and 8th and the Bureau for Economic Research will release its second quarter inflation expectations survey on June 8th. Source: Business Day, May 31.

China, SA Conclude Draft Agreement to Restrict Textile Exports
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¶4. China and South Africa concluded a draft agreement to restrict Chinese textile exports to South Africa according to the Chinese government. The agreement had been circulated by South Africa's Department of Trade and Industry to its textile industry for comment, said Zhou Yabin, the Director-General for West Asia and Africa in the Ministry of Commerce. China is addressing local concerns about strong competition from Chinese textile imports by encouraging its textile enterprises to reduce their investments and production in China and to focus more on high-quality textiles and clothing as this would reduce direct competition with African producers of lower-quality goods. Making conditional loans is another incentive to encourage more production abroad. Zhou believed the concerns of textile producers, especially in South Africa, lay behind the hesitation by the SA Customs Union (SACU) countries to conclude negotiations for a China-SACU free trade area. An agreement was supposed to have been reached by the end of 2004, but negotiations are still continuing. Source: Business Report, May 30.

SA Trade Deficit Reaches R2.4 Billion

¶5. South Africa's trade deficit improved slightly to R2.4 billion in April compared to March's deficit of R2.9 billion, according to the South African Revenue Service (SARS). A Reuters poll of economists forecasted a trade deficit of R2 billion. Exports decreased by 11.5% m/m to R26.5 billion in April from R29.95 billion in March, while imports declined by 11.9% m/m to R28.93 billion from R32.8

billion in March. Domestic demand is relatively healthy with the current level of imports close to the average monthly increase of around R29 billion in 2005. The cumulative deficit for the first four months of the year amounted to R17.13 billion versus a deficit of R4.9 billion in the same period in 2005. Exports of mineral products, machinery, precious metals and chemicals and imports of vehicles, machinery, mineral products and instruments declined during April. The South Africa Reserve Bank's import cover ratio (which excludes foreign currency held by all other monetary authorities) increased to 20.2 weeks (5 months) in April from 17.4 weeks (4.3 months) in March. Source: Standard Bank Foreign Trade Alert and Reuters, May 31.

Eskom Spending a Brake on Increased SA Growth
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¶6. In testimony to Parliament, Eskom officials admitted that underspending on new generating capacity presented a constraint on increased growth in the economy and meant that its electrification program might fail to meet the program's targets. Brian Dames, a managing director at Eskom's enterprises division, said that Eskom's R84 billion ($13 billion using 6.5 rands per dollar) capital expenditure plans were based on an expectation of only 4% economic growth. With 4% growth, Eskom (a government-controlled energy utility) expected electricity would increase by 2.3%. The South African government is aiming for 6% growth which would mean that electricity demand growth to reach 4.4%. At the World Economic Forum (WEF) in Cape Town, Steve Lennon, Eskom's Managing Director for Resources and Strategy, said that South Africa's target of universal electrification by 2012 could only be met if Eskom spent an additional R9 billion ($1.4 billion) on the program. From 1994 to 2004, more than 3 million homes had been electrified. Rural and semi-urban areas have the most gaps in coverage. Source: Business Report, June 1.

Manufacturing Recovers

¶7. Investec's South Africa's Purchasing Managers Index (PMI) rose to 57.6 in May from April's 54.3, confirming a recovery in the manufacturing sector due to buoyant

domestic demand growth. It was the third month in 2006 that the index has been above the 50 level that divides growth and contraction, after dropping below 50 in January and February. The price component of the PMI rose to 68.8 in May from 66.9 in April, suggesting the recent increase in producer inflation (PPI) may continue. The business activity component rose to 60.3 from 55.5 in April, with new sales orders increasing to 63.7 from 58.1. More positive was the employment index reaching 50.3 in April from 47.9, further evidence that the economy was creating jobs. Respondents' short-term expectations regarding general business conditions improved to 69.9 in May from 68.1 in April. Source: Reuters, June 1.

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